

## GENERAL INFORMATION

*The Community Reinvestment Act (“CRA”) requires each federal financial supervisory agency to use its authority when examining financial institutions subject to its supervision to assess the institution’s record of meeting the credit needs of its entire community, including low- and moderate-income neighborhoods, consistent with the safe and sound operation of the institution. Upon conclusion of such examination, the agency must prepare a written evaluation of the institution’s record of meeting the credit needs of its community.*

*This document is an evaluation of the CRA performance of the Citizens State Bank of St. James, St. James, Minnesota, prepared by the Federal Reserve Bank of Minneapolis, the institution’s supervisory agency, as of June 30, 1997. The agency rates the CRA performance of an institution consistent with the provisions set forth in Appendix A to 12 CFR Part 228.*

**INSTITUTION’S CRA RATING:** This institution is rated “Outstanding.”

Several factors support the bank’s outstanding rating. First, the bank lends to small businesses and to borrowers of many different income levels. Second, the bank maintains a strong loan-to-deposit ratio that is supplemented by significant community development lending activity. Finally, the bank is proactive and participates in many community development investments and programs that provide a high level of service benefiting low- and moderate-income individuals. These investments and services contribute to the outstanding rating.

## **DESCRIPTION OF INSTITUTION**

The bank is able to meet the community's credit needs effectively based on its size and product offerings. This is the first evaluation by the Federal Reserve Bank of Minneapolis since the bank became a member of the Federal Reserve System ("System") effective February 1, 1996. Previously, the bank was evaluated by the Federal Deposit Insurance Corporation ("FDIC"). The bank was rated satisfactory in helping to meet the credit needs of its community at its previous CRA evaluation. The bank operates a full-service office in St. James, Minnesota. The bank does not own or operate any automated teller machines or branches.

According to its March 31, 1997, Report of Condition ("ROC"), the bank's assets totaled approximately \$47 million. The March 31, 1997, ROC indicates the bank's major loan category is agricultural lending, which comprises 37% of its loan portfolio. The balance of the bank's lending portfolio is composed of 33% commercial, 18% residential real estate, 9% consumer, and 3% other loans. The composition of the bank's loan portfolio reflects the demand for the specific types of loans in the assessment area.

The bank offers a variety of products that serve the credit needs of area residents, including agricultural, consumer, business, community development, and government-guaranteed loans. In addition, the bank provides residential real estate loans for construction, purchasing, refinancing, and improving homes. The bank offers government-guaranteed loan programs sponsored by the Small Business Administration, Department of Veterans Affairs, Farm Service Agency, Rural Development Agency - Rural Housing Service, Federal Housing Administration, Minnesota Housing Finance Agency ("MHFA") First-Time Home Buyer Program, MHFA Fix-up Fund, MHFA Home Energy Program, and Minnesota Agriculture Best Program. The bank's loan products appear appropriate for its community's credit needs.

## **DESCRIPTION OF CITIZENS STATE BANK OF ST. JAMES' ASSESSMENT AREA**

The bank's assessment area is defined as Watonwan County, Minnesota. Located in south-central Minnesota, the county comprises block numbering areas ("BNA") 9501, 9502, and 9503. All three BNAs are designated middle income. The city of St. James and the bank are in BNA 9502. According to 1990 U.S. census figures, Watonwan County has a population of 11,682. St. James is the county seat for Watonwan County, and it is the largest community in the assessment area. According to 1990 census data, it has a population of 4,364. St. James is located approximately 35 miles southwest of Mankato, Minnesota, and roughly 35 miles north of the Iowa border. Other communities in the assessment area include Madelia, Lewisville, Odin, Butterfield, La Salle, and Darfur.

CRA divides income levels into four categories: low, moderate, middle, and upper. Because the bank's assessment area is not in a metropolitan statistical area, the categorization of a borrower or BNA's income is determined relative to the statewide nonmetropolitan median family income. Low-income individuals have incomes of less than 50% of the statewide nonmetropolitan median family income, while moderate-income individuals have incomes of at least 50% but less than 80% of this amount. The regulation defines a middle-income person as one with an income of at least 80% but less than 120% of the statewide nonmetropolitan median family income. An individual with an income that is 120% or more of the statewide nonmetropolitan median family income is considered an upper-income person. BNAs are classified using similar categories based on the level of the median family income in the geography.

As mentioned, all three BNAs in the bank's assessment area are middle income. According to 1990 census data, the assessment area's median family income is \$27,633, while its median household income is \$20,000. For comparison, the median family and median household income figures for nonmetropolitan areas in Minnesota are \$28,933 and \$23,627, respectively. There are 3,099 families and 4,483 households in the assessment area. Approximately 8% of the families and 12% of the households in the assessment area have incomes below the poverty level. The following table summarizes the distribution of household and family incomes for the assessment area.

<b>ASSESSMENT AREA POPULATION BY INCOME LEVEL</b>				
<b>Unit of Measure</b>	<b>Low Income</b>	<b>Moderate Income</b>	<b>Middle Income</b>	<b>Upper Income</b>
Households Compared to Median Household Income	23%	17%	22%	38%
Families Compared to Median Family Income	18%	21%	28%	33%

The economy in the bank's assessment area is strongly related to agriculture. According to community contacts and bank management, the diversity of farm products includes cash crops such as corn, soybeans, and alfalfa and livestock-derived products such as hogs and cattle. There are also a few dairy operations. In 1996, the agricultural economy was good due to favorable market prices.

Major employers in the area include three food-processing plants that employ several hundred workers. Bank management and the community contacts commented that much of the local industry is agriculture-dependent. Besides the food processors, there is a trucking operation, a farming cooperative, and grain storage facilities. Other major employers that are not agriculturally dependent include a truck accessories manufacturer and a precision tool manufacturer. Community contacts indicated that jobs in the community are primarily low-paying jobs.

Examiners contacted one local individual familiar with economic development issues and one state government representative as part of the bank's CRA evaluation. Examiners used information from these contacts as well as information from bank management to help evaluate the bank's CRA performance.

## **CONCLUSIONS WITH RESPECT TO PERFORMANCE CRITERIA**

The bank's performance in meeting the credit needs in its assessment area is outstanding. Much of the analysis on the following pages is based on a statistical sample of 90 commercial, 86 agricultural, and 52 residential real estate loans originated by the bank in the six months preceding the evaluation. The criteria detailed below were reviewed to determine this rating. In assigning the overall rating, the greatest weight was placed on the assessment of lending to borrowers of different income levels and businesses of different sizes. The bank's community development lending and investment and service activities further enhance the strong lending performance. These factors most closely measure the bank's success in meeting the credit needs of all segments of its community.

### **LOAN-TO-DEPOSIT RATIO ANALYSIS**

The bank's loan-to-deposit ratio is high and exceeds the standards for satisfactory performance. The bank's quarterly net loan-to-deposit ratio has been consistently high and ranged between 79% to 83% since

membership. Based on March 31, 1997, Uniform Bank Performance Report ("UBPR") data, the bank's net loan-to-deposit ratio is 79%, which places the institution in the 89th percentile of its national peer group. Based on ROC data for the five calendar quarters since membership, the quarterly average of the bank's net loan-to-deposit ratio is 81%. The following chart summarizes the bank's net loan-to-deposit ratio and its components since the membership date.

<b>DATE</b>	<b>NET LOANS (IN THOUSANDS)</b>	<b>DEPOSITS (IN THOUSANDS)</b>	<b>NET LOAN-TO-DEPOSIT RATIO</b>
March 31, 1996	\$31,451	\$38,289	82%
June 30, 1996	\$31,623	\$39,476	80%
September 30, 1996	\$31,986	\$38,403	83%
December 31, 1996	\$34,557	\$43,136	80%
March 31, 1997	\$32,730	\$41,349	79%

The bank's net loans and deposits have increased since membership. Using quarterly ROC data since March 31, 1996, net loans and deposits have increased approximately \$1.2 million and \$3.1 million, respectively.

A substantial number of real estate loans were sold on the secondary market since the bank's membership in the System. The bank's secondary market lending included many loans to low- and moderate-income borrowers under the MHFA programs.

According to bank management, the fluctuations of net loans and deposits during 1996 were due to normal expansion of small business and agricultural operating demands. The bank also extensively marketed its residential real estate loan products during that time. Between December 31, 1996, and March 31, 1997, the decrease in net loans and deposits is due to the normal cycle of loan paydowns on agricultural credits.

The bank's quarterly average net loan-to-deposit ratio is greater than its major bank competitors. The following table, based on quarterly ROC data, identifies the asset sizes and quarterly average loan-to-deposit ratios for the bank and its competitors.

<b>BANK AND LOCATION</b>	<b>TOTAL ASSETS AS OF MARCH 31, 1997 (IN THOUSANDS)</b>	<b>QUARTERLY AVERAGE LOAN-TO-DEPOSIT RATIO</b>
Citizens State Bank of St. James St. James, MN	\$47,247	81%
Farmers State of Madelia, Inc. Madelia, MN	\$37,320	79%
State Bank of La Salle La Salle, MN	\$28,596	67%
Odin State Bank Odin, MN	\$24,538	71%
First National Bank at St. James St. James, MN	\$20,118	45%
Merchants State Bank Lewisville, MN	\$11,620	79%

As the table above shows, the subject bank is larger than its competitors and its quarterly average net loan-to-deposit ratio is higher than any of the listed ratios of the competitor banks in the assessment area. Additionally, there is aggressive competition for real estate loans from a local savings bank and for agricultural loans from a Farm Service co-op. As reflected by the competitor data, it appears the demand for credit in the assessment area is strong. It is apparent that local banks are willing to extend credit to fulfill the needs of local residents, farms, and businesses. Based on the bank's high loan-to-deposit ratio and secondary market lending, comparison to competitors, and its UBPR ranking, the bank's loan-to-deposit ratio exceeds the standards for satisfactory performance.

#### LENDING IN THE ASSESSMENT AREA

The bank's lending activity within its assessment area meets the standards for satisfactory performance. A review of a statistical sample of loans originated by the bank in the six months preceding the evaluation reveals that a majority of its loans were made inside the assessment area. The following table shows the percentage of loans within the assessment area based on total number and amount in each major loan category.

<b>PERCENTAGE OF LOANS IN THE ASSESSMENT AREA</b>		
Major Loan Product Lines	Total Number of Loans	Total Amount of Loans
Residential Real Estate	76	66
Commercial	73	56
Agricultural	84	70

As noted in the table, the majority of the bank's loans were within the assessment area. Based on these concentrations of loans within the assessment area, the bank's lending performance for this category meets the standards for satisfactory performance.

#### LENDING TO BORROWERS OF DIFFERENT INCOME LEVELS AND TO BUSINESSES OF DIFFERENT SIZES

The bank's level of lending to individuals of different incomes and to businesses and farms of different sizes exceeds the standards for satisfactory performance. As discussed previously, CRA classifies income levels into four categories: low, moderate, middle, and upper. The median household and family incomes for the bank's assessment area are \$20,000 and \$27,633, respectively.

The following table shows the percentage of residential real estate loans made to borrowers of different income levels.

<b>DISTRIBUTION OF LOANS BY BORROWER INCOME LEVEL IN THE ASSESSMENT AREA*</b>				
<b>Loan Type</b>	<b>Low Income</b>	<b>Moderate Income</b>	<b>Middle Income</b>	<b>Upper Income</b>
<b>RESIDENTIAL REAL ESTATE</b>				
Percentage of Total Loans	22	27	24	27
Percentage of Total Loan Amounts	14	26	32	28
*Income level is determined based on Minnesota's 1997 nonmetropolitan median family income of \$38,400				

The data in the table indicate that the bank provided 49% of the residential real estate loans to low- and moderate-income individuals. This percentage compares very favorably with the percentage of low- and moderate-income households and families in the bank's assessment area. As previously mentioned, the approximate percentages of the assessment area's households and families classified as low and moderate income are 40% and 39%, respectively. This penetration is particularly noteworthy since low-income families have annual incomes below \$19,200 and moderate-income families have incomes between this level and \$30,720. These incomes limit the ability of many borrowers to afford housing.

It should be noted that the bank originates and sells residential real estate loans on the secondary market, including many loans to low- and moderate-income borrowers under MHFA loan programs. Residential real estate loans that are sold on the secondary market often follow more stringent underwriting criteria than loans that the bank maintains.

CRA defines small farms and businesses as those with less than \$1 million in gross annual revenues. All of the bank's commercial and agricultural borrowers reviewed are small businesses and small farms. In the review of commercial borrowers, 97% of the reviewed loans were in amounts less than \$100,000. Similarly, 88% of agricultural loans in the sample were in amounts less than \$100,000 and 11% of the reviewed agricultural loans were for amounts greater than \$100,000 and below \$250,000.

Based on the strong level of residential real estate lending to low- and moderate-income borrowers compared with the representation of those individuals in the community and the number of small farm and business loans extended, the bank exceeds the standards for satisfactory performance.

#### GEOGRAPHIC DISTRIBUTION OF LOANS

As previously discussed, the BNAs that make up the bank's assessment area are classified middle income. There are no low-, moderate-, or upper-income BNAs in the assessment area. Bank management indicated the low- and moderate-income residents are not concentrated in any particular area but are dispersed throughout the assessment area. Approximately 85% of the small farm, 98% of the small business, and 85% of the residential real estate loans in the sample are concentrated in the BNA where the bank is located. The low level of lending in the remaining BNAs seems to be the result of heavy bank competition in the assessment area.

## INVESTMENTS

Since the bank's membership in the System, it has engaged in many investments that are noteworthy for CRA purposes. The bank has made the several investments in the community and assessment area. First, the bank provided a small grant to the Region 9 Development Commission. The purpose of this commission is to provide support for small business development. Similarly, the bank gave a small amount of grant money to Southeast Minnesota Initiative Fund ("SEMIF"), an organization whose function is to support business development for start-up, minority-, and women-owned and -operated businesses.

Finally, the bank invested a significant amount for the St. James Economic Development Authority ("EDA") Function Bond for multiunit (fourplex) housing for elderly and low- and moderate-income residents. According to a community contact, the bank took a leadership role in the instigation of this project.

## SERVICES

The bank has provided many services deemed to be qualified services and that enhance its CRA rating. The following service and service-related activities were initiated since the bank's System membership. First, the bank has provided volunteer instructors for MHFA Home Stretch Workshops. These workshops are intended for homebuyer training, typically for first-time and low- to moderate-income people who want to buy a home but are not sure how to go about it.

In July 1996, the bank adopted new hours that increased the lobby hours on Thursday from 5:30 p.m. to 6:00 p.m. and initiated Saturday lobby hours from 8:00 a.m. to noon. In addition, drive-up and walk-up hours were increased to 8:00 a.m. to 6:00 p.m. Monday through Friday and 8:00 a.m. to noon on Saturday.

The bank provides FDIC brochures, credit card brochures, and residential application guides in Spanish. The Hispanic population has increased recently, which creates the need for bilingual materials.

The bank played a leadership role in helping the city of St. James receive funds from the MHFA's Minnesota City Participation Program ("MCP"). This program is intended to provide low-interest loans to assist low- and moderate-income, first-time homebuyers. Some borrowers who are eligible for the MCP also may be eligible for MHFA's Homeownership Assistance Fund, which offers an interest-free second mortgage to assist first-time homebuyers with down payment or monthly payment costs. In St. James, funding for the MCP can be used for the purchase of a new or existing house.

The bank also provides leadership and other volunteer support for the EDA's Housing Plan, which focuses on elderly and low- and moderate-income people. The bank president is a member of the EDA and a very strong supporter of its functions.

Finally, the bank plays a very active role with the Spirit of St. James, a volunteer organization of nine committees that focuses on the development and revitalization of the downtown and other parts of the community. The president of the bank serves on the finance committee and is the organization's treasurer.

### GENERAL

The evaluation did not reveal any violations of the substantive provisions of the fair housing and fair lending laws and regulations. The evaluation did reveal a technical, isolated violation of the Equal Credit Opportunity Act's Regulation B. The bank has not received any CRA complaints since its membership into the System.



## **PUBLIC DISCLOSURE**

June 30, 1997  
Date of Evaluation

## **COMMUNITY REINVESTMENT ACT PERFORMANCE EVALUATION**

Citizens State Bank of St. James  
Name of Depository Institution

092753600000  
Identification Number of Institution

St. James, Minnesota  
Address of Institution

Federal Reserve Bank of Minneapolis  
250 Marquette Avenue  
Minneapolis, Minnesota 55401-2171

NOTE: This evaluation is not, nor should it be construed as, an assessment of the financial condition of this institution. The rating assigned to this institution does not represent an analysis, conclusion, or opinion of the federal financial supervisory agency concerning the safety and soundness of this financial institution.